Supreme Court, U.S.
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No. 01-800

In The
Supreme Court of the United States

KAREN HOWSAM, individually and as Trustee for the E. Richard Howsam, Jr. Irrevocable Life Insurance Trust dated May 14, 1982,

Petitioner,

v.

DEAN WITTER REYNOLDS, INC., a Delaware corporation,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

REPLY BRIEF FOR THE PETITIONER

ALAN C. FRIEDBERG
Counsel of Record
PENDLETON, FRIEDBERG, WILSON & HENNESSEY, P.C.
303 E. 17th Avenue, #1000
Denver, CO 80203-1263
303-839-1204
Counsel for Petitioner

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

TABLE OF CONTENTS

	Page
ARGUMENT IN REPLY	1
I. RULE 10304 MUST BE APPLIED BY ARBITRATORS	1
A. DWR'S ARGUMENT FOR COURT DETERMINATION OF "ALL RESTRICTIONS ON THE SCOPE OF ARBITRATION" IS UNSUPPORTED BY PRECEDENT	1
B. THE PARTIES' INTENT TO ARBITRATE MATTERS WITHIN THE SCOPE OF THE AGREEMENT IS PRESUMED	4
C. ANALYSIS OF TEXT, STRUCTURE, AND PURPOSE SHOWS THAT THE SIX YEAR RULE DOES NOT INVOKE THE ARBITRABILITY QUESTION	6
1. The Split Among Courts Demonstrates The Inherent Ambiguity of Rule 10304	6
2. Textual and Contextual Analysis Confirms That Rule 10304 Is To Be Applied By Arbitrators	9
3. Rule 10304 Is A Procedural Timeliness Rule, Not An Arbitrability Rule	14
D. ARBITRATORS ARE CAPABLE OF APPLYING RULE 10304	14
E. POLICY CONSIDERATIONS CONFIRM THAT RULE 10304 IS FOR THE ARBITRATORS TO APPLY	16

TABLE OF CONTENTS – Continued

Page

F. THE NASD'S STATEMENTS REGARDING WHO APPLIES RULE 10304 DO NOT SUPPORT DWR'S POSITION; THE SEC SUPPORTS HOWSAM'S POSITION .. 18

II. CERTIORARI WAS PROVIDENTLY GRANTED 19

CONCLUSION..... 20

TABLE OF AUTHORITIES

Page

FEDERAL CASES

Armco Employees Indep. Fed'n v. AK Steel Corp., 252 F.3d 854 (6th Cir. 2001).....3, 4

AT&T Technologies, Inc. v. Communications Workers of America, 475 U.S. 643 (1986).....19

Conroy v. Merrill Lynch, Pierce, Fenner & Smith, 899 F. Supp. 1471 (W.D.N.C. 1995).....16

Cogswell v. Merrill Lynch, Pierce, Fenner & Smith, 78 F.3d 474 (10th Cir. 1996)..... 7

Deal v. U.S., 508 U.S. 129 (1993).....13

Dean Witter Reynolds v. Byrd, 470 U.S. 213 (1985) 15

Dean Witter Reynolds v. McCoy, 853 F. Supp. 1023 (E.D. Tenn. 1994), *aff'd*, 70 F.3d 1271 (6th Cir. 1995).....16

FDA v. Brown & Williamson Tobacco Corp., 529 U.S. 120 (2000).....10

First Options of Chicago v. Kaplan, 514 U.S. 938 (1995).....1, 6, 9

FSC Sec. Corp. v. Freel, 14 F.3d 1310 (8th Cir. 1994) 8

General Drivers, Warehousemen & Helpers, Local Union 89 v. Moog Louisville Warehouse, 852 F.2d 871 (6th Cir. 1988) 3, 4

Humphrey v. Prudential Sec., No. CA-92-178-2, *slip op.* at 10 (E.D. Va. Jan. 6, 1993), *appeal dismissed*, 4 F.3d 313 (4th Cir. 1993)..... 8

Int'l Union of Operating Eng'rs v. Flair Builders, Inc., 406 U.S. 487 (1972)..... 5

TABLE OF AUTHORITIES – Continued

Page

J.E. Liss & Co. v. Levin, 201 F.3d 848 (7th Cir. 2000) 17

John Wiley & Sons, Inc. v. Livingston, 376 U.S. 543 (1964) 2, 3, 4

Kidder, Peabody & Co. v. Brandt, 131 F.3d 1001 (11th Cir. 1997) 17

Market Co. v. Hoffman, 101 U.S. 112 (1879) 11

Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52 (1995) 6, 9

Merrill Lynch, Pierce, Fenner & Smith v. Cohen, 62 F.3d 381 (11th Cir. 1995) 7, 17

Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, 473 U.S. 614 (1985) 2, 15

Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1 (1983) 1, 2, 5, 9

Osler v. Ware, 114 F.3d 91 (6th Cir. 1997) 17

O'Neel v. Nat'l Ass'n of Sec. Dealers, Inc., 667 F.2d 804 (9th Cir. 1982) 7

PaineWebber Inc. v. Allen, 888 F. Supp. 53 (E.D. Va. 1993), *aff'd mem.*, 45 F.3d 427 (4th Cir. 1995) 8

PaineWebber Inc. v. Bybyk, 81 F.3d 1193 (2nd Cir. 1996) 7, 11

Painewebber Inc. v. Elahi, 87 F.3d 589 (1st Cir. 1996) 7, 9, 13

PaineWebber, Inc. v Farnam, 870 F.2d 1286 (7th Cir. 1989) 7

PaineWebber, Inc. v. Hartmann, 921 F.2d 507 (3d Cir. 1990) 7, 8, 13

TABLE OF AUTHORITIES – Continued

Page

Painewebber, Inc. v. Hofmann, 984 F.2d 1372 (3d Cir. 1993) 17

Raceway Park v. Local 47, SEIU, 167 F.3d 953 (6th Cir. 1999) 3

Rodriquez de Quijas v. Shearson/American Express, 490 U.S. 477 (1989) 15

Roney & Co. v. Kassab, 981 F.2d 894 (6th Cir. 1992) 7, 16

Shearson/American Express v. McMahon, 482 U.S. 220 (1987) 15

Smiley v. Citibank (S.D.), N.A., 517 U.S. 735 (1996) 8, 9

Smith Barney Shearson, Inc. v. Boone, 47 F.3d 750 (5th Cir. 1995) 7

Textron Lycoming Reciprocating Engine Div. v. United Auto., 523 U.S. 653 (1998) 13

U.S. v. Amer. Trucking Ass'ns, 310 U.S. 534 (1940) 13

Udall v. Tallman, 380 U.S. 1 (1965) 19

Unemployment Comp. Comm'n v. Aragon, 329 U.S. 143 (1946) 19

United Steelworkers of America v. Warrior & Gulf Navigation Co., 363 U.S. 574 (1960) 2, 4

Weisgram v. Marley Co., 528 U.S. 440 (2000) 13

Wis. Dep't of Health & Family Servs. v. Blumer, 534 U.S. 473 (2002) 9

TABLE OF AUTHORITIES – Continued

Page

STATE CASES

Barnett Sec. v. Faerber, 648 So. 2d 265 (Fla. App. 2d Dist. 1995) 8

Bayley v. Fox, 671 N.E.2d 133 (Ind. App. 1996) 7

Citibank v. Crowell, Weedon & Co., 5 Cal.Rptr.2d 906 (Cal. App. 2d Dist. 1992) 8

Corporate Secs. Group v. Lind, 753 So. 2d 151 (Fla. App. 4th Dist. 2000), *review dismissed*, 789 So. 2d 340 (Fla. 2001) 8

Gaines v. Fin. Planning Consultants, Inc., 857 S.W.2d 430 (Mo. App. 1993) 7

Kennedy, Cabot & Co. v. Nat'l Ass'n of Sec. Dealers, Inc., 49 Cal.Rptr.2d 66 (Cal. App. 2d Dist. 1996) 8

Levine v. Advest, Inc., 714 A.2d 649 (Conn. 1998) 7

Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Havird, 518 S.E.2d 48 (S.C. App. 1999) 8

Mid-State Sec. Corp. v. Edwards, 706 A.2d 773 (N.J. Super. App. Div. 1998) 8

Ohio Co. v. Stambaugh, 1998 Ohio App. LEXIS 2583 (Ohio App., Clark Co., June 12, 1998) 7

Shahan v. Staley, 932 P.2d 1345 (Ariz. App. 1996) 7

Smith Barney Shearson Inc. v. Sacharow, 689 N.E.2d 884 (N.Y. 1997) 7

Smith Barney, Inc. v. Bardolph, 509 S.E.2d 255 (N.C. App. 1998) 8

Smith Barney, Inc. v. Keeney, 570 N.W.2d 75 (Iowa 1997) 7

TABLE OF AUTHORITIES – Continued

Page

Smith Barney, Inc. v. Painters Local Union No. 109 Pension Fund, 579 N.W.2d 518 (Neb. 1998) 7

Todorov v. Alexander, 600 N.W.2d 418 (Mich. App. 1999) 7

Weston Secs. Corp. v. Aykanian, 703 N.E.2d 1185 (Mass. App. 1998) 7

FEDERAL STATUES AND REGULATIONS

9 U.S.C. § 1, *et seq.* 1, 9, 16

59 Fed. Reg. 39373 (Aug. 2, 1994) 19

63 Fed. Reg. 588 (Jan. 6, 1998) 17, 18, 19

67 Fed. Reg. 19464 (April 19, 2002) 19, 20

OTHER AUTHORITIES

Mason, C. Thomas, III, *Irreducible Disagreements: The Six-Year Eligibility Rule Revisited*, 1 Securities Arbitration 1997, 557-759 (PLI, Corp. Law & Pract. Conf. Handbook Series, #B4-7195, July 1997) 7, 17

Rule 10101, NASD Code of Arbitration Procedure 10, 11, 12

Rule 10104, NASD Code of Arbitration Procedure 10, 12

Rule 10301, NASD Code of Arbitration Procedure 10, 11, 12

Rule 10304, NASD Code of Arbitration Procedure ..... *passim*

TABLE OF AUTHORITIES – Continued

Page

Rule 10305, NASD Code of Arbitration Procedure 10, 11

Rule 10324, NASD Code of Arbitration Procedure 7, 8, 11, 12, 19

Rule 10336, NASD Code of Arbitration Procedure 10, 12

Rush, Pamela Jeanne Turbow, *Securities Arbitration: The Six-Year Eligibility Rule*, 26 Stetson L. Rev. 329 (Fall, 1996) 17

Unif. Arbitration Act (2000), 7 U.L.A., Part 1 (Supp. 2002) 14

ARGUMENT IN REPLY

I. RULE 10304 MUST BE APPLIED BY ARBITRATORS

A. DWR'S ARGUMENT FOR COURT DETERMINATION OF "ALL RESTRICTIONS ON THE SCOPE OF ARBITRATION" IS UNSUPPORTED BY PRECEDENT

DWR contends that the presumption that courts will decide issues of arbitrability applies to "[a]ll restrictions on the scope of arbitration." Resp. Br. 13. However, DWR has not identified any case which applies that presumption to any question other than (1) whether the parties are bound by a valid arbitration agreement and (2) whether the subject matter of the dispute falls within the agreement.

In *First Options of Chicago v. Kaplan*, 514 U.S. 938 (1995), the parties had not signed an agreement to arbitrate anything, let alone arbitrability. Unlike *First Options*, the parties in this case did sign an arbitration agreement. This case therefore raises questions answered by *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1 (1983), in which the parties agreed to arbitrate, but disagreed over which merits-related disputes were covered. In such a case, the courts apply a strong presumption in favor of arbitration:

> The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an

> allegation of waiver, delay, or a like defense to arbitrability.[1]

Guidance is also found in *John Wiley & Sons, Inc. v. Livingston*, 376 U.S. 543, 558-559 (1964), in which the Court said "[r]efusal to order arbitration of subjects which the parties have not agreed to arbitrate does not entail the fractionating of disputes about subjects which the parties do wish to have submitted."

DWR mistakenly contends that Howsam and the SEC argue for a *per se* rule that time limits can never be enforced by courts (Resp. Br. 15, 18) or that Howsam is trying "to manufacture some *heightened* presumption with respect to timeliness" (Resp. Br. 19). To the contrary, Howsam and the SEC simply argue that the ordinary presumption in favor of having arbitrators decide issues in the first instance applies to time limits, in the absence of express language stating otherwise. *See* SEC Br. 11-12, 16, 17 n.5, 19.

DWR further errs in arguing that Howsam's and the SEC's "position is not based on the parties' expressed intent." Resp. Br. 15. DWR is unable to point to anything that comes remotely close to an agreement by the parties that timeliness issues should be decided by a court rather than arbitrators. Indeed, it is DWR which advocates "[d]eparting from the parties' expressed intent in favor of artificial presumptions untethered to intent" (Resp. Br. 29) by trying to avoid the ordinary understanding of the clause mandating arbitration of "all controversies" between the parties.

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[1] *Moses H. Cone*, 460 U.S. at 24-25. *See also Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*, 473 U.S. 614, 626 (1985); *United Steelworkers of America v. Warrior & Gulf Navigation Co.*, 363 U.S. 574, 582-583 (1960).

DWR argues that the concept of "subject matter" arbitrability is inherently indeterminate. But its position that "all restrictions on the scope of arbitration" are arbitrability issues for court determination is far more difficult to administer. Presumably, such restrictions could entail payment of arbitration filing fees, timely submission of briefs, or compliance with other procedural requirements, all of which are within the province of arbitrators to decide.

DWR invokes *General Drivers, Warehousemen & Helpers, Local Union 89 v. Moog Louisville Warehouse*, 852 F.2d 871, 874 (6th Cir. 1988), in support of its position that "subject matter" can include a time limitation. In stating that "[a]t least one circuit has construed the 'subject matter' of a dispute in precisely that way" (Resp. Br. 16), DWR totally ignores the fact that other panels of the Sixth Circuit have disapproved the holding in *Moog*; *e.g., Raceway Park v. Local 47, SEIU*, 167 F.3d 953 (6th Cir. 1999); *Armco Employees Indep. Fed'n v. AK Steel Corp.*, 252 F.3d 854 (6th Cir. 2001).

In the first paragraph of *Raceway Park*, the court described *Moog* as "a decision with which we disagree" but were forced to follow "despite strong misgivings." 167 F.3d at 954. The court further stated that *Moog* "represents a grave departure from Supreme Court doctrine mandating that issues of procedural arbitrability be determined by arbitrators, not judges," *citing John Wiley,* 167 F.3d at 954. In a section entitled ***"Moog's* MISFORTUNE,"** the court wrote,

> We find that there is no rational basis on which to distinguish between those issues which the Supreme Court in *John Wiley & Sons* deemed to be procedural, and thus reserved for the

> arbitrator, and the issue considered by this Court in both *Moog* and the present matter.

Id. at 962.

In *Armco*, a later Sixth Circuit panel flatly refused to apply *Moog*, choosing instead to follow *John Wiley*, holding that the question of timeliness must be submitted to the arbitrator. 252 F.3d at 861.

B. THE PARTIES' INTENT TO ARBITRATE MATTERS WITHIN THE SCOPE OF THE AGREEMENT IS PRESUMED

DWR appears to contend that whether a particular issue is a question of "arbitrability" turns on the parties' intent. Resp. Br. 18, 19, 26. While this Court has held that the parties' intent controls who decides whether claims are arbitrable, where the parties have agreed to arbitrate all controversies, only the most "forceful" evidence of intent to exclude a dispute from arbitration will prevail. *Warrior & Gulf*, 363 U.S. 584-585. It is DWR, not Howsam, who suggests a new unfamiliar test requiring multi-layered inquiries into the parties' intent.

At page 17 of its brief, DWR, discussing *John Wiley*, states that,

> In sum, the Court considered a timeliness issue as an 'arbitrability' issue for judicial resolution pursuant to the parties' expressed intent; it did not use an artificial 'subject matter'/procedure distinction to override that intent, as petitioner and the SEC urge here.

DWR confuses the Court's discussion of whether or not the union's claim arose before expiration of a collective bargaining agreement with discussion of whether the union's claims were procedurally timely. The Court held that the former issue was for the court to decide and left the latter to the arbitrators. In Howsam's case, no one has suggested

that the 1992 Agreement had expired or for any other reason did not cover Howsam's claims.

DWR's attempt to distinguish *Int'l Union of Operating Eng'rs v. Flair Builders, Inc.*, 406 U.S. 487 (1972), is equally unavailing. DWR, with no support from the text of *Flair Builders*, states that the Court,

> assumed that restrictions on the timeliness of disputes can present 'arbitrability' issues for judicial resolution, but determined that the parties in that case had expressed an intent to arbitrate timeliness because (unlike here) they had not incorporated into their agreement a provision excluding untimely disputes from arbitration.

Resp. Br. 17. To the contrary, if any "assumption" by the Court can be gleaned from *Flair Builders*, it is that for issues of timeliness, the usual presumption in favor of submission of issues to arbitrators applies once it is determined that the parties entered into a valid arbitration agreement covering the subject matter of the dispute. Nothing in Rule 10304 supports DWR's position that the parties agreed it was to be applied by courts rather than arbitrators. J.A. 48. As DWR itself states, "[t]he 'clear and unmistakable' presumption applies to whether the parties agreed to submit arbitrability to arbitrators, not to whether an issue is an arbitrability issue in the first place." Resp. Br. 18.

DWR's attempt to minimize the effect of the statement in *Moses H. Cone* that "doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability," is also unconvincing. 460 U.S. at 24-25. DWR argues that the quoted language "only confirms . . . that non-'subject matter' limitations, including timeliness limitations, are *not* governed by a special

standard." Resp. Br. 19. That statement contradicts its position that "all restrictions on the scope of arbitration" are governed by the special *First Options* presumption that parties do not intend to arbitrate arbitrability.

DWR's discussion of *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52 (1995), is also off the mark. DWR suggests that this Court's resolution of whether punitive damages were available in arbitration is inconsistent with a "subject matter" limitation on arbitrability issues. Resp. Br. 18. However, as DWR points out in its brief, *Mastrobuono* addressed only whether punitive damages were available, not who should decide whether they were arbitrable. Resp. Br. 41. *Mastrobuono* came to this Court after arbitrators had determined in the first instance that they could award punitive damages. The process was consistent with Howsam's and the SEC's position that DWR can seek judicial review of the arbitrators' application of Rule 10304, but cannot preempt the arbitrators' determination by antecedent court action.

C. ANALYSIS OF TEXT, STRUCTURE, AND PURPOSE SHOWS THAT THE SIX YEAR RULE DOES NOT INVOKE THE ARBITRABILITY QUESTION

1. The Split Among Courts Demonstrates The Inherent Ambiguity of Rule 10304

The split in the circuits arises from two opposing constructions of Rule 10304 and similar rules of other SROs. One holds that the rule is a substantive limitation on the arbitrators' powers and therefore a matter of threshold arbitrability. The other holds that the rule is procedural and therefore within the jurisdiction of the arbitrators. Five federal circuits and at least two state appellate courts have published decisions adopting the securities industry's position that the rule presents an

issue of arbitrability.[2] However, a New York appellate court concluded that a customer agreement requiring arbitration of "any and all controversies" evidenced intent to send questions of arbitrability to the arbitrators. That court buttressed its conclusion by finding that Rule 10324 is a "clear and unmistakable" expression of "the parties' intent and commitment to arbitrate the issue of arbitrability." *Sacharow*, 689 N.E.2d at 888; J.A. 48.

On the other side of the issue, four federal circuits and nine state appellate courts have held that the six year rule is a matter for the arbitrators and not a substantive limitation on arbitrability.[3] In addition, the Eighth Circuit

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[2] *See PaineWebber, Inc. v. Hartmann*, 921 F.2d 507 (3d Cir. 1990); *Roney & Co. v. Kassab*, 981 F.2d 894 (6th Cir. 1992); *PaineWebber, Inc. v Farnam*, 870 F.2d 1286 (7th Cir. 1989); *Cogswell v. Merrill Lynch, Pierce, Fenner & Smith*, 78 F.3d 474 (10th Cir. 1996); *Merrill Lynch, Pierce, Fenner & Smith v. Cohen*, 62 F.3d 381 (11th Cir. 1995); *Todorov v. Alexander*, 600 N.W.2d 418 (Mich. App. 1999); *Smith Barney Shearson Inc. v. Sacharow*, 689 N.E.2d 884 (N.Y. 1997). A third state has an unpublished opinion consistent with this view: *Ohio Co. v. Stambaugh*, 1998 Ohio App. LEXIS 2583 (Ohio App., Clark Co., June 12, 1998).

C. Thomas Mason's comprehensive study of the six year rule provides a history of the rule, analyzes its meaning and application, and examines every publicly available court decision dealing with the six year rule from its inception through May 1997. *Irreducible Disagreements: The Six-Year Eligibility Rule Revisited*, 1 Securities Arbitration 1997, 557-759 (hereafter Mason, *Irreducible Disagreements).* (Mr. Mason provided substantial material for this brief.)

[3] *See Painewebber Inc. v. Elahi*, 87 F.3d 589 (1st Cir. 1996); *PaineWebber Inc. v. Bybyk*, 81 F.3d 1193 (2nd Cir. 1996); *Smith Barney Shearson, Inc. v. Boone*, 47 F.3d 750 (5th Cir. 1995); *O'Neel v. Nat'l Ass'n of Sec. Dealers, Inc.*, 667 F.2d 804 (9th Cir. 1982); *Shahan v. Staley*, 932 P.2d 1345 (Ariz. App. 1996); *Levine v. Advest, Inc.*, 714 A.2d 649 (Conn. 1998); *Bayley v. Fox*, 671 N.E.2d 133 (Ind. App. 1996); *Smith Barney, Inc. v. Keeney*, 570 N.W.2d 75 (Iowa 1997); *Weston Secs. Corp. v. Aykanian*, 703 N.E.2d 1185 (Mass. App. 1998); *Gaines v. Fin. Planning Consultants, Inc.*, 857 S.W.2d 430 (Mo. App. 1993); *Smith Barney, Inc. v. Painters Local Union No. 109 Pension Fund*, 579 N.W.2d 518 (Neb.

(Continued on following page)

held that regardless of whether the rule is substantive or procedural, Rule 10324 "is *a 'clear and unmistakable' expression of [the parties'] intent to leave the question of arbitrability to the arbitrators.*" *FSC Sec. Corp. v. Freel*, 14 F.3d 1310, 1312-1313 (8th Cir. 1994) (emphasis added).

The split among the circuits and state appellate courts demonstrates that Rule 10304 and similar SRO rules are ambiguous. Numerous panels of learned, qualified, and thoughtful judges from five federal circuits, appeals courts in nine states, and many trial courts have disagreed with the language quoted by DWR from *Hartmann*. Resp. Br. 20.

This Court has rejected the argument that language is unambiguous where courts have been so fractionalized in its interpretation. As the Court stated in *Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 739 (1996), "[i]n light of the two dissents . . . and . . . the opinion . . . creating the

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1998); *Mid-State Sec. Corp. v. Edwards*, 706 A.2d 773 (N.J. Super. App. Div. 1998); *Smith Barney, Inc. v. Bardolph*, 509 S.E.2d 255 (N.C. App. 1998). *See also Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Havird*, 518 S.E.2d 48 (S.C. App. 1999) (review dismissed at the request of the parties, appellate opinion vacated).

The D.C. Circuit has not examined the issue. The Fourth Circuit has not decided the question in a published opinion; its statements in dicta and unpublished opinions conflict: contrast *Humphrey v. Prudential Sec.*, No. CA-92-178-2, *slip op.* at 10 (E.D. Va. Jan. 6, 1993), *appeal dismissed*, 4 F.3d 313 (4th Cir. 1993), with *PaineWebber Inc. v. Allen*, 888 F. Supp. 53 (E.D. Va. 1993), *aff'd mem.*, 45 F.3d 427 (4th Cir. 1995). Florida state courts appear to be in conflict: compare *Barnett Sec. v. Faerber*, 648 So. 2d 265 (Fla. App. 2d Dist. 1995), with *Corporate Secs. Group v. Lind*, 753 So. 2d 151 (Fla. App. 4th Dist. 2000), *review dismissed*, 789 So. 2d 340 (Fla. 2001). California Courts have spoken only in dicta and also appear to be in conflict: compare *Citibank v. Crowell, Weedon & Co.*, 5 Cal.Rptr.2d 906 (Cal. App. 2d Dist. 1992), with *Kennedy, Cabot & Co. v. Nat'l Ass'n of Sec. Dealers, Inc.*, 49 Cal.Rptr.2d 66 (Cal. App. 2d Dist. 1996).

conflict that has prompted us to take this case, it would be difficult indeed to contend that the word 'interest' . . . is unambiguous with regard to the point at issue here." *See also Wis. Dep't of Health & Family Servs. v. Blumer*, 534 U.S. 473 (2002) (similar, citing *Smiley*).

Because the six year rule is ambiguous, courts should apply the strong presumption in favor of arbitration. "[W]hen a court interprets [ambiguous] provisions in an agreement covered by the FAA, 'due regard must be given to the federal policy favoring arbitration, and ambiguities as to the scope of the arbitration clause itself resolved in favor of arbitration.'" *Mastrobuono*, 514 U.S. at 62. "[S]ilence or ambiguity about the question 'whether a particular merits-related dispute is arbitrable because it is within the scope of a valid arbitration agreement'" is construed so as to direct the dispute to arbitration. *First Options*, 514 U.S. at 944-5; also *Moses H. Cone*, 460 U.S. at 24-25.

As the First Circuit stated in *Elahi*, "the signing of a valid agreement to arbitrate the merits of the subject matter in dispute presumptively pushes the parties across the 'arbitrability' threshold; we will then presume that other issues relating to the substance of the dispute or the procedures of arbitration are for the arbitrator." 87 F.3d at 599.

2. Textual and Contextual Analysis Confirms That Rule 10304 Is To Be Applied By Arbitrators

Principles of statutory interpretation can assist in understanding Rule 10304 and its place within the NASD Code.

> [A] reviewing court should not confine itself to examining a particular statutory provision in isolation. The meaning – or ambiguity – of certain

> words or phrases may only become evident when placed in context. It is a 'fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme.' A court must therefore interpret the statute 'as a symmetrical and coherent regulatory scheme,' and 'fit, if possible, all parts into an harmonious whole.'

FDA v. Brown & Williamson Tobacco Corp., 529 U.S. 120, 132-133 (2000) (citations omitted). The Court should therefore look at how Rule 10304 fits into the Code as a whole.

The NASD Code of Arbitration Procedure is organized into four parts:

> Series 1: Administrative Provisions (Rules 10100-10106)
>
> Series 2: Industry and Clearing Controversies (Rules 10200-10216)
>
> Series 3: Uniform Code of Arbitration (Rules 10300-10336)
>
> Series 4: Mediation Rules (Rules 10400-10406)

Rule 10101 is entitled "Matters Eligible for Submission." It adopts the Code for arbitration of "any dispute, claim, or controversy arising out of or in connection with the business of any member of the Association . . . (c) between or among members or associated persons and public customers, or others." J.A. 47.

Rules 10301-10336 are rules of arbitration *procedure* for the parties and arbitrators to follow. They deal with pleadings, selection of arbitrators, composition of panels, discovery, hearing procedures, awards, fees, and other related topics. Rule 10301 states, "[a]ny dispute, claim, or controversy *eligible for submission under the Rule 10100*

Series between a customer and a member and/or associated person arising in connection with the business of such member or in connection with the activities of such associated persons shall be arbitrated under this Code . . . " (emphasis added). Rule 10304 is an instruction *to the arbitrators* regarding timeliness. The placement of Rule 10304 in Series 3 of the Code rather than Series 1, supports Howsam's and the SEC's position that it is meant to be a procedural matter for the arbitrators to decide. In that same vein, Rule 10305, entitled "Dismissal of Proceedings," authorizes the arbitrators to dismiss proceedings under certain circumstances.

Rule 10324 expressly empowers the arbitrators "to interpret and determine the applicability of all provisions under this Code and to take appropriate action to obtain compliance with any ruling by the arbitrator(s)." J.A. 48. This power clearly includes interpreting and applying Rules 10301, 10304, and 10305. "Nothing in the NASD Code removes [Rule 10304] from the ambit of [Rule 10324]." *Bybyk*, 81 F.3d at 1202.

Rules of construction for statutes and contracts advise against interpretations which would make some provisions surplusage. " '[A] statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant.' This rule has been repeated innumerable times." *Market Co. v. Hoffman*, 101 U.S. 112, 115-116 (1879). Rule 10301(a), which repeats language in Rule 10101 and refers expressly to it, would be redundant without recognition that the 10300 series provides procedural instructions to arbitrators and parties.

Examining and analyzing the phrases relating to "eligibility" for "submission" makes more sense against the backdrop of the division of the Code into its parts. Rule 10301(d) provides that class actions and claims by

class members are not eligible for arbitration except where a class member has opted out of the class. Rule 10301 does not alter Rule 10101's definition of arbitrability. Rather, it provides procedural rules. Similarly, Rule 10301(a)(1)-(3) provides that claims involving terminated, expelled, or defunct members are ineligible for submission unless the customer agrees in writing to arbitrate. Again, the rule is one of procedure rather than arbitrability, even though words of eligibility are used.

DWR's references to Rule 10104, which provides for appointment of arbitrators for "any matter which shall be eligible for submission under this Code," and Rule 10301 help prove the point. Resp. Br. 35. Rule 10104 closely follows Rule 10101, which lists matters eligible for submission. Both are contained in Series 1. DWR concludes, erroneously, that Rule 10104 "contemplates that eligibility [under Rule 10304] is determined *before* arbitrators are appointed, not by the arbitrators themselves." DWR argues that "[w]hen the NASD wished to make a limited exception to this rule, it did so expressly" in Rule 10301, which grants "arbitrators authority to determine whether certain class action-type claims are eligible for submission." By placing the six year rule in Series 3, along with Rule 10301, the NASD also placed authority to determine eligibility under the six year rule with the arbitrators. By doing so, it demonstrated its intent that the time limitation did not implicate "arbitrability" and would be subject to interpretation and application by the arbitrators under Rule 10324. Otherwise, why not include the six year rule in Rule 10101 or in Series 1?

The fallacy of DWR's position is again demonstrated by its reference to Rule 10336(a) which provides for an amount-in-controversy limitation for claims "eligible to be heard by a single arbitrator." Resp. Br. 21. Rule 10336 "allows" parties with claims of $50,000 to $200,000 to elect a single arbitrator instead of a panel of three. DWR's

argument that "eligible" in that context equates to "arbitrable" reduces itself to an absurdity and demonstrates clearly that "eligible" does not always mean "arbitrable."

Looking at the words "eligible" and "submission" in the dictionary, as the Third Circuit did in *Hartmann* (Resp. Br. 20), without looking to their textual surroundings and practical application, violates the teachings of this Court. In *U.S. v. Amer. Trucking Ass'ns,* 310 U.S. 534, 542 (1940), the Court counseled against taking "a few words from their context and with them thus isolated to attempt to determine their meaning . . . ." Similarly, the Court has said, "it is a 'fundamental principle of statutory construction (and, indeed, of language itself) that the meaning of a word cannot be determined in isolation, but must be drawn from the context in which it is used.'" *Textron Lycoming Reciprocating Engine Div. v. United Auto.*, 523 U.S. 653, 657 (1998), *citing Deal v. U.S.*, 508 U.S. 129, 132 (1993).

The word "submission" has a number of meanings in differing contexts. In ordinary legal parlance, "submission" means tendering a cause to the adjudicator after presentation of evidence and/or legal argument. *See, e.g., Weisgram v. Marley Co.*, 528 U.S. 440, 448 n.4 (2000) ("[m]otions for judgment as a matter of law may be made at any time before submission of the case to the jury"). Appellate cases are taken under "submission" after oral arguments, not when the notices of appeal are filed. The word "submission" in Rule 10304 reasonably refers to "submission for full adjudication of the merits, rather than submission for preliminary determinations, such as whether the claim is time-barred, or whether the appropriate fee was paid, or whether the claim was submitted on the proper forms." *Elahi*, 87 F.3d at 600.

3. Rule 10304 Is A Procedural Timeliness Rule, Not An Arbitrability Rule

DWR argues that Rule 10304's time limitation is not a statute of limitation or repose and was adopted by the NASD and other SROs to avoid arbitration of stale claims. Resp. Br. 22-23. Regardless, it is still a timeliness rule. The fact that it is not coextensive with statutes of limitation says nothing about whether or not it should be considered a question of arbitrability. Because the Rule relates to timeliness in asserting a claim rather than to the character of the underlying claim, and because it requires a detailed understanding of the underlying claim, it should be considered a question presumptively for the arbitrators to decide.

Section 6(c) of the Uniform Arbitration Act (2000), provides that arbitrators "shall decide whether a condition precedent to arbitrability has been fulfilled . . . ." Unif. Arbitration Act (2000) § 6(c), 7 U.L.A. 12 (Supp. 2002). The drafters of the Act "intended to incorporate the holdings of the vast majority of state courts and the law that has developed under the FAA that, . . . issues of procedural arbitrability, *i.e.*, whether prerequisites such as time limits, notice, laches, estoppel, and other conditions precedent to an obligation to arbitrate have been met, are for the arbitrators to decide." *Id.* at 13 cmt. 2.

D. ARBITRATORS ARE CAPABLE OF APPLYING RULE 10304

DWR cites the NASD's statement that "the *securities industry believed* that the inherently equitable nature of arbitration posed a greater risk that arbitrators might not strictly apply legal defenses such as statutes of limitation" as if such belief were authoritative. Resp. Br. 24. That argument is particularly surprising in light of the fact that arbitration is imposed on investors by the securities industry, including DWR, which succeeded in convincing

this Court in *Dean Witter Reynolds v. Byrd*, 470 U.S. 213 (1985), and subsequent cases, to enforce customer arbitration agreements.

The arbitral fora available to investors are SRO's, such as the NASD, which select and train their arbitrators. Nevertheless, DWR repeatedly suggests that arbitrators are not to be trusted to follow the law and fairly to resolve disputes. Resp. Br. 24, 32, 34 n.7. DWR even cynically suggests that arbitrators will not properly apply Rule 10304 because they have a financial incentive to hear cases on their merits rather than dismiss them early on. Resp. Br. 32, 34 n.7. There is no evidence that NASD arbitrators depend for their living on the honoraria they receive. Most are employed full-time in other pursuits or are retired. None gets rich arbitrating.

This Court rejected arguments that arbitrators were unqualified in *Shearson/American Express v. McMahon*, 482 U.S. 220, 232 (1987),

> In *Mitsubishi*, for example, we recognized that arbitral tribunals are readily capable of handling the factual and legal complexities of antitrust claims, notwithstanding the absence of judicial instruction and supervision. Finally, we have indicated that there is no reason to assume at the outset that arbitrators will not follow the law; although judicial scrutiny of arbitration awards necessarily is limited, such review is sufficient to ensure that arbitrators comply with the requirements of the statute.

Citations omitted. The Court in *McMahon* held that arbitrators are capable of applying the federal securities laws and the RICO act. After *Byrd*, *McMahon*, and *Rodriquez de Quijas v. Shearson/American Express*, 490 U.S. 477 (1989), the securities industry, and DWR, should be estopped from arguing that arbitrators are not competent to apply Rule 10304.

E. POLICY CONSIDERATIONS CONFIRM THAT RULE 10304 IS FOR THE ARBITRATORS TO APPLY

DWR makes the grandiose statement that, "[b]y denigrating the parties' expressed intent, petitioner would jeopardize the rights of all parties to arbitration agreements, particularly (and ironically) consumers." Resp. Br. 28. First, the parties' "expressed intent" was to arbitrate "all controversies" between them arising out of securities transactions. Second, the statement is irrelevant to the question of who decides whether claims fall within a six year period. DWR, as it frequently does in its brief, confuses the parties' "intent" not to arbitrate claims more than six years old with a purported intent to have the courts decide which claims are timely. Howsam respectfully submits that a decision by this Court in her favor will not jeopardize the rights of all parties to arbitration agreements, including consumers.[4]

DWR further contends that Howsam's and the SEC's argument that judicial determination of Rule 10304 timeliness issues would thwart FAA policies by slowing down the dispute resolution process "is both irrelevant and incorrect." Resp. Br. 30. It is neither. It is relevant because this Court has repeatedly held that one goal of the FAA is to encourage speedy and efficient dispute resolution. Howsam does not advocate that this goal take precedence over enforcing arbitration agreements according to their terms. Simply put, nothing in the parties' arbitration

[4] DWR's professed concern for customers is ironic in light of its and the securities industry's position that if a claim is not "arbitrable" under Rule 10304, it is also not litigable in court. *See, e.g., Dean Witter Reynolds v. McCoy*, 853 F. Supp. 1023, 1025 (E.D. Tenn. 1994), *aff'd*, 70 F.3d 1271 (6th Cir. 1995); *Roney & Co.*; *Conroy v. Merrill Lynch, Pierce, Fenner & Smith*, 899 F. Supp. 1471, 1476 (W.D.N.C. 1995), and cases cited therein.

agreement provides for judicial resolution of ancillary procedural issues such as timeliness.

Howsam's and the SEC's position is also correct. There can be no doubt that antecedent judicial proceedings under Rule 10304 result in extra costs and delays. The NASD itself recognizes this when it said, "[u]nder the proposed rule, customers (investors) will be assured that their claims will be heard either in court or in arbitration, and that they will not be subjected to *repeated, costly, time-consuming, and indeterminate battles* over the eligibility of their claim for arbitration." 63 Fed. Reg. 588, 592 (Jan. 6, 1998) (emphasis added). Jurisdictions holding that the six year rule is an arbitrability limitation require trial courts to hold fact-intensive "mini-trials" to determine when claims accrued. *See, e.g., Cohen*; *Painewebber, Inc. v. Hofmann,* 984 F.2d 1372, 1379-1382 (3d Cir. 1993); *Kidder, Peabody & Co. v. Brandt*, 131 F.3d 1001, 1004 (11th Cir. 1997).

Rule 10304 does not provide a "bright-line" for quick and easy determination. Courts have disagreed on how to determine the date from which the six year period begins to run. In *Osler v. Ware*, 114 F.3d 91, 93 (6th Cir. 1997), the court stated that accepting the transaction-date argument "would create situations in which certain claims would be barred before they even arose. Needless to say, we refuse to interpret the 'occurrence or event' language . . . in this manner." In *J.E. Liss & Co. v. Levin*, 201 F.3d 848, 851 (7th Cir. 2000), the court said "Rule 10304 does not bar a claim that arises within the six-year period merely because the securities involved in the claim were bought more than six years before the claim was filed." *See also* Mason, *Irreducible Disagreements*, 703-707, 712-716.

The NASD itself has not consistently interpreted the six year period as beginning to run on the date of the transaction. In 1991, the NASD Director of Arbitration was authorized by the National Arbitration Committee to use the date of discovery of the wrong-doing as the beginning date. Rush, *Securities Arbitration: The Six-Year*

Eligibility Rule, 26 Stetson L. Rev. 329, 344-345 (Fall, 1996). The rule itself speaks of the "occurrence or event giving rise to the act or dispute, claim or controversy." It could have stated, but did not, that the time begins to run from the date of the purchase or sale or other complained-of transaction.

The NASD has commented that,

> some courts, arbitrators, and the Director permitted certain claims to be arbitrated even though they appeared to be based on events more than six years old under a theory akin to equitable tolling. Other courts, some arbitrators, and, several years ago, the Director, applied a 'bright-line' transaction date test holding that the date of the transaction was determinative of the eligibility of a claim and that the limit could not be tolled.

63 Fed. Reg. at 590-591.

DWR's argument that it "defies common sense to subject parties to the time and expense of full arbitration proceedings, and only then to determine whether those proceedings were valid" (Resp. Br. 32) fails to take into account that the arbitrators' decision may obviate any need for judicial intervention. Furthermore, judicial review does not entail a retrial, but is simply a review under a deferential standard. Court application of the six year rule before consideration by the arbitrators is akin to submitting motions to dismiss to appellate courts before trial courts have considered them.

F. THE NASD'S STATEMENTS REGARDING WHO APPLIES RULE 10304 DO NOT SUPPORT DWR'S POSITION; THE SEC SUPPORTS HOWSAM'S POSITION

DWR's assertion that the NASD interprets its rules as calling for court enforcement of Rule 10304 is wrong. Resp.

Br. 37. The cited passage from 59 Fed. Reg. 39373, 39374 simply states the NASD's incorrect reading of *AT&T Technologies, Inc. v. Communications Workers of America*, 475 U.S. 643 (1986), as of July 1994. More recently, in 63 Fed. Reg. at 590, the NASD recognized that there is "significant confusion about who should decide eligibility issues. Some courts have held that eligibility was for the courts to decide; others have held that the arbitrators could decide the issue. In some cases, the courts have declined to decide the issue . . . ."

The SEC, which approves the NASD's rules after notice and comment (SEC Br. 1), asserts that Rule 10324 clearly indicates that arbitrators are to decide Rule 10304 questions. *See* 67 Fed. Reg. 19464, 19466 n.11 (April 19, 2002). The SEC's interpretation should be given substantial weight by the Court. *Cf. Udall v. Tallman*, 380 U.S. 1, 16 (1965) ("[w]hen faced with a problem of statutory construction, this Court shows great deference to the interpretation given the statute by the officers or agency charged with its administration"); *Unemployment Comp. Comm'n v. Aragon*, 329 U.S. 143, 153 (1946) ("[t]o sustain the Commission's application of this statutory term, we need not find that its construction is the only reasonable one, or even that it is the result we would have reached had the question arisen in the first instance in judicial proceedings").

II. CERTIORARI WAS PROVIDENTLY GRANTED

DWR urges the Court to dismiss Howsam's petition as improvidently granted because the NASD is attempting to amend Rules 10304 and 10324. Proposed changes to the rules have been pending for nearly a decade without any final action. Even though the proposed changes to Rules 10304 and 10324 have now been separated from changes to other rules, the SEC considered it necessary to submit the proposed rule changes for additional public

comment. The NASD and the SEC continue to evaluate comments and there is no certainty that the proposal will survive in its present form or that the SEC will approve it. The SEC, in 67 Fed. Reg. 19464, poses nine questions which indicate a number of concerns with the language and effect of the proposed rule changes. There is no basis for DWR's statement that "the SEC is expected to approve it." Resp. Br. 45.

Regardless of whether the proposed amendments are enacted, there are underlying issues of whether timeliness limitations contained in arbitration forum rules or in contracts are for courts or arbitrators to adjudicate.

Most importantly to Howsam, she and other public investors are entitled to relief under the existing rules. They should not have to continue to face expensive and time-consuming litigation of matters properly submitted to arbitration.

CONCLUSION

For the reasons stated in Howsam's and the SEC's briefs, this Court should hold that Rule 10304 is for the arbitrators to apply and reverse the judgment of the Tenth Circuit.

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August 21, 2002

Respectfully submitted,

ALAN C. FRIEDBERG
Counsel of Record
PENDLETON, FRIEDBERG,
WILSON & HENNESSEY, P.C.
303 E. 17th Avenue, #1000
Denver, CO 80203-1263
303-839-1204
Counsel for Petitioner